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Remarks delivered by
Mr. Cleviston Haynes, Governor (Ag), Central Bank of Barbados
at the
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on
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Master of Ceremonies,

Distinguished guests, Ladies and Gentlemen

Let me begin by congratulating the CHSB for hosting this important conference that seeks to empower our leaders with the tools to manage risk in the dynamic environment in which we operate today. Understanding and adapting to emerging risks and opportunities is essential if firms are to compete successfully in an increasingly technology driven competitive space where barriers to entry are being eroded rapidly. Firms which formerly competed in the domestic market only can now, with a touch of a button, compete abroad or conversely face competition from abroad.

It is in this context that I am honoured, therefore, to present this morning on the theme ***Perspectives on Growth in the Caribbean.*** As a policymaker, I am acutely aware that the long term success of our business sector depends in part on how quickly and effectively we are able to create a policy framework that facilitates growth, builds confidence, stimulates innovation and encourages new investment. This is essential because some of the industries that have served us well in the past may not be viable in the new globalised environment. Our capacity to grow strong competitive firms and develop new industries will therefore be critical. Our responsiveness to emerging risks, whether as policymakers or as producers, is therefore crucial. Understanding the challenges which each stakeholder faces is key to the long term sustainability of the economy and the development of strong competitive enterprises.

In my presentation, therefore, I propose to share some insights on the recent growth experience in the economies of the CARICOM region. I will use the recent Barbados experience to assist in illustrating the need for a sound macroeconomic framework to underpin sustainable growth.

Discussions on growth in Caribbean economies are now topical. Such discussions are often prefaced by the recognition that these economies are constrained by their small size in terms of land mass and population and are vulnerable to economic shocks and natural catastrophes. In addition, Caribbean economies are distinguished by an absence of diversity in the goods produced and a heavy dependence on imports and a limited range of export products.

Regional economies are not homogeneous as evidenced, for example, by the characterisation of some jurisdictions as commodity based producers and others as services based or the differences in the land mass of Guyana and Suriname relative to the rest of CARICOM. However, economic size remains an impediment in much that we do. The most recent example has been the loss of correspondent banking relationships by some of our countries. This may affect a jurisdiction's ability to send and receive international payments, or drive some payment flows into the unregulated sector, with potential consequences on international trade, growth, financial inclusion, as well as the stability and integrity of the financial system.

On average small economies have been the most affected by the reduction in the number of foreign correspondent banks serving banks in these countries as the absence of a sufficient volume of business may deter correspondent banks, given the fixed costs associated with opening and maintaining a relationship.

The challenge therefore is how do we overcome these perceived constraints to generate sufficient economic growth that reduces unemployment and poverty and raises the level of socioeconomic development while enabling a sustained increase in living standards across the region. The Human Development Index Report for 2016 suggests that CARICOM economies have made progress in this regard with only Haiti, the largest economy on a population size basis, being classified as having a low level of human development while Guyana has a medium level of development. Led by Barbados and The Bahamas, all other CARICOM countries were deemed to have high levels of development.

The progress in human development reflects the emphasis which Caribbean nations have placed on human development but in some respects it is remarkable because rates of economic growth in the region have witnessed a marked decline since the 1960s. In a recent CDB Working Paper entitled "**Enhancing Productivity and Growth in the Caribbean**" it was noted that "the average annual growth rate fell from 6% in the 1960s to less than 1% in recent years." A 2015 IDB study points out that that for the preceding 25 years Caribbean economic growth was 1.7% compared to 3.7% for the world and 4.6% for emerging markets.

The secular shift from robust growth to the current anaemic performance that is well below the global average has been attributed to several well-known factors such as the oil price increases in the 1970s, the loss of preferential trading arrangements, reduced access to official development assistance, the impact of recessions in the region's main trading partners and natural disasters.

The recent global financial crisis is but the latest of these exogenous factors that has had a profound impact on regional economies which are yet to recover sufficiently to achieve pre-crisis growth levels. In the early stage of the post-crisis period, growth was driven by the commodity-based producers but, over the last three years, activity in the service-based economies has exceeded, if only modestly, that in commodity producers as commodity prices have weakened. To put this in perspective, while the average growth for the region recovered to 1.7% in 2014, regional output declined by 0.7% in 2016 due to the weak performance of commodity-based economies.

Forecasts for 2017 and 2018 are for a moderate recovery as the world economic outlook remains positive and the regional economic outturn continues to be driven by international economic developments. However, the regional underperformance suggests that that economic growth cannot be linked solely to activity in our main trade partners. Rather it reflects the impact of the structural factors identified earlier as well as the slow adaptation to the changing global environment. Of particular note is that the region as a whole ranks in the bottom half of most of the World Bank's Ease of Doing business indicators. This is a source of concern as foreign investment is a vital element of regional growth strategies.

Notwithstanding the exogenous shocks which these economies face, it is increasingly clear that a sound macroeconomic framework is a prerequisite for sustainable growth. At the same time, structural weaknesses often undermine resilience and compromise the buffers necessary to cope with economic shocks.

Several regional economies face chronic external current account imbalances which are funded by a combination of foreign direct investment, public sector borrowing and the depletion of international reserves. Persistent fiscal deficits resulting from deliberate fiscal strategies or the inadvertent outcomes resulting from economic or natural shocks have led to the significant build-up of sovereign debt in several jurisdictions.

These trends tend to place pressure on foreign exchange holdings in fixed rate countries and exchange rates in floating rate economies and have forced several regional governments to embark on adjustment programmes designed to address these imbalances of large deficits and high debt ratios. Fiscal space to use countercyclical policies have been eroded as high interest costs have resulted in the need for large primary surpluses in some countries in order to restore balance to the public finances.

It is in this context that I refer to the Barbadian experience. The Barbadian economy has encountered multiple policy challenges in the aftermath of the global financial crisis, as policy makers in a low growth environment have sought to preserve exchange rate stability through the maintenance of adequate foreign exchange buffers, to alter the path of public sector debt dynamics and to create a macroeconomic environment for long-term sustainable growth. The macroeconomic strategy has focused on demand management so as to reduce outward foreign exchange flows while alleviating the financing pressures that have been placed on government by large fiscal imbalances. This strategy has been buttressed by measures to enhance the economy's long term competitive position through fiscal incentives for the foreign exchange earning and saving sectors.

The Barbadian economy registered relatively buoyant economic activity between 2004 and 2008 when substantial foreign direct investment flows had a favourable impact on the construction sector. However, since the crisis, economic output has been depressed, induced initially by the dampening of global economic activity with its adverse spill-over effects on the key tourism and international business services sectors as well as on private sector investment inflows.

In response, policy makers avoided any significant counter cyclical thrust, given the size and openness of the economy and its vulnerability to foreign exchange leakages that have the ability to undermine the credibility of the exchange rate peg.

A sharp downturn in 2009 when declining activity in the tourism and construction sectors spread to the rest of the economy has been followed by tepid growth. The protracted weakness has been influenced by the implementation of fiscal adjustment measures targeted at reducing imbalances in the accounts of central government and public enterprises, slowing the surge in public sector indebtedness and containing the outflow of international reserves.

Improved tourist arrivals since 2015 have raised hopes of a more vibrant recovery but the slow recovery in foreign investment flows associated with planned infrastructural projects continued to contain capital formation which remained below the level needed for sustained growth. For example, the average capital formation as a share of GDP was only 13.0% for 2010-2015 compared to 18.2% in 2008 when the financial crisis started.

As indicated, Government's policy goals were targeted towards fiscal consolidation. Initial efforts to contain the central government deficit before 2013 were influenced by the favourable size of the foreign reserves buffer and on-going access to external capital markets. However, the sharp deterioration in the public finances in FY 2013-14 led Government to embark on a 19 month fiscal adjustment programme in second half of 2013. Despite some progress, Government recently embarked on a more aggressive adjustment effort, including addressing interest costs on selected debt on a voluntary basis, to reflect current borrowing constraints.

The impact of the fiscal developments was manifold. First, fiscal adjustment attempted to compensate for the substantial loss in taxes from foreign sources by substituting with domestic taxes. As a result, sequential reforms were made to the personal income tax and property taxes, new taxes were introduced to stabilise revenue and the value added tax was reformed and the rate increased.

Secondly, potential growth enhancing capital expenditure absorbed much of the initial non-interest expenditure adjustment. However, state enterprises were able to cushion the impact on growth through their capital works programmes. However, since some of these enterprises lack the financial capacity to service the ensuing debt, central government is expected to absorb the costs over the medium term.

Thirdly, the persistence of large deficits and rising debt led to deterioration in the sovereign credit rating, with adverse effects on access to capital markets at reasonable costs. Increased reliance on domestic financing while servicing debt has added to the depletion of reserves.

Fourth, government encountered cash flow difficulties that encumbered its ability to make payments on a timely basis, including to some of its public enterprises.

Fifth, policy makers were forced to review how longstanding entitlement programmes, particularly for education and health, should be financed in an environment in which financial resources were insufficient to meet demand.

Sixth, policy makers have had to review the size of the public sector, its scope of activities and its efficiency in delivering its services. Jobs were cut from the public sector roll in 2013 and steps taken to identify agencies which could be merged to avoid potential duplication of services. This review is on-going. In addition, some state assets have been identified for divestment, creating resources to ease short term financing flows.

Some of the challenges being experienced in Barbados are being replicated across the region. Deficits, debt and access to low cost finance are interrelated. It is important for us to recognise that every dollar of the fiscal deficit has to be financed or arrears will accumulate. The sale of state assets, when judiciously applied, can enhance cash flow by providing one-time revenue. But in general, only productive assets can be quickly sold for what there are worth, while the sale of such assets may have, inter alia, competition, relative prices, income distribution and foreign exchange effects. Moreover, divestment does not substitute for the need for fiscal adjustment.

Against this backdrop, what therefore can we conclude about the future growth prospects for the region? We need to address our macroeconomic imbalances. Historically, regional governments have used deficit financing to stimulate economic activity. However, the large debt burdens which many face and which have led investors to shift away from providing financing could impact this strategy. This does not mean that our economies cannot grow, but we may need to rely more on private sector flows to drive economic activity, at least in the short term. We need more investment spending to drive our productive capacities and raise the ratio of capital spending as a proportion of GDP.

Current budgetary constraints raise the question of how will governments allocate their resources in the future. Social expenditures? Capacity building infrastructure?

However, while macroeconomic stability is necessary it is unlikely by itself to be sufficient to propel regional economies forward. We will need to inter alia raise productivity levels through process improvements and innovation. We need to take advantage of ICT technology and, as old sectors fade, we have to encourage new sectors such as alternative energy, design services, cultural industries, animation and software development, for these are areas in which size need not be an impediment.

Our future can be bright but there will be some bumps along the way. Our ability to recognise and act on these challenges in as expeditious a manner as possible will allow us to achieve our long term objectives.